

No. 76-1798

Supreme Court, U. S.

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In the Supreme Court of the United States

OCTOBER TERM, 1977

ARTHUR J. HOMANS, PETITIONER

v.

SECURITIES AND EXCHANGE COMMISSION

ON PETITION FOR A WRIT OF CERTIORARI TO THE
UNITED STATES COURT OF APPEALS FOR THE
SECOND CIRCUIT

BRIEF FOR THE SECURITIES AND EXCHANGE
COMMISSION IN OPPOSITION

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**BRIEF FOR THE SECURITIES AND EXCHANGE
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OPINIONS BELOW

The opinion of the court of appeals (Pet. App. 1a-9a)¹ is reported at 546 F. 2d 1044. The opinion of the district court (Pet. App. 1b-61b) is not officially reported.

JURISDICTION

The judgment of the court of appeals was entered on December 16, 1976. A timely petition for rehearing and suggestion for rehearing *en banc* was denied on March

¹"Pet. App." refers to petitioner Homans' appendix. "Pet." refers to the Homans' petition. "C.A. App." refers to the appendix in the court of appeals, a copy of which will be lodged in this Court.

25, 1977 (Pet. App. 1c-2c). A petition for a writ of certiorari was filed on June 17, 1977. The jurisdiction of this Court is invoked under 28 U.S.C. 1254(1).

QUESTION PRESENTED

Whether an attorney who assisted in his client's illegal distribution of unregistered securities by providing purchasers with an opinion that the transactions were legal, although he knew they were not, was properly enjoined from further activities violating or aiding or abetting violations of the registration provisions of the Securities Act of 1933.

STATUTE INVOLVED

Section 5(a) of the Securities Act of 1933, 48 Stat. 77, as amended, 15 U.S.C. 77e(a), is set forth at Pet. App. Id.

STATEMENT

In an injunction action brought by the Securities and Exchange Commission in the United States District Court for the Southern District of New York, petitioner, the general counsel of Universal Major Industries Corporation (UMI) from 1959 through 1973, was found to have aided and abetted in the unlawful distribution of some 3,000,000 shares of UMI stock without registration, in violation of Section 5 of the Securities Act of 1933 (Pet App. 2a, 32b, 54b). Petitioner had stated in numerous letters to stock transferees that the transaction was legal (Pet. App. 5a) or enclosed a letter to that effect from UMI's "special counsel" (Pet. App. 3a-4a).

The district court found that petitioner "had direct knowledge of the fact that his client was engaged in an illegal distribution of common stock" in at least some of these transactions, and that he "knew that his opinion would be used to further those illegal distributions"

(Pet. App. 46b). It further found that if he had exercised due diligence in other transactions, "he would have known that the transactions upon which he was being asked to furnish an opinion * * * also involved illegal distributions of unregistered securities," and that it was "reckless for him not to have looked behind the representations" made to him (*ibid.*). Pointing out that petitioner continued as "attorney for four other public corporations subject to the federal securities laws" (Pet. App. 49b) and intended to continue in the practice of securities law (Pet. App. 50b), the court enjoined petitioner from violating or aiding and abetting future violations of the registration provisions of the Securities Act (C.A. App. A-216 to A-217).

The court of appeals affirmed, noting (Pet. App. 7a) that "the District Court found that [petitioner] in some circumstances knew and in other circumstances had reason to know that his client was engaging in illegal transactions with the aid of [petitioner's] letters and that [petitioner's] acts were performed with knowledge or reckless disregard of the truth."

ARGUMENT

The decision of the court of appeals is correct and the petition raises no questions warranting further review.

1. Petitioner does not dispute that the court of appeals correctly upheld the district court's determination that the petitioner aided and abetted a violation of Section 5 of the Securities Act of 1933. He contends (Pet. 10, 11-12), however, that an injunction may not issue against a person who aids and abets a Section 5 violation, such as an attorney, as distinguished from "'primary' violators named in the Securities Act, e.g., issuers, officers and directors

of issuers, underwriters, etc.”² He also contends that if such an injunction may issue there must be a finding of *scienter*, rather than negligence (Pet. 18).

It has long been recognized that in both enforcement actions brought by the Commission and private actions for damages, liability appropriately may be imposed on persons who aid and abet the securities laws violations of others. *Rochez Brothers, Inc. v. Rhoades*, 527 F. 2d 880, 886 (C.A. 3); *Woodward v. Metro Bank of Dallas*, 522 F. 2d 84, 94 (C.A. 5); *Securities and Exchange Commission v. Management Dynamics, Inc.*, 515 F. 2d 801, 811 (C.A. 2); *Securities and Exchange Commission v. Coffey*, 493 F. 2d 1304, 1315-1317 (C.A. 6), certiorari denied, 420 U.S. 908; *Securities and Exchange Commission v. Spectrum, Ltd.*, 489 F. 2d 535, 541 (C.A. 2); *Securities and Exchange Commission v. National Bankers Life Insurance Company*, 448 F. 2d 652 (C.A. 5), affirming, 324 F. Supp. 189, 194 (N.D. Tex.); *Securities and Exchange Commission v. Barraco*, 438 F. 2d 97, 99-100 (C.A. 10); *Batten & Co. v. Securities and Exchange Commission*, 345 F. 2d 82, 84 (C.A. D.C.).³ It was noted in *Barraco, supra*, 438 F. 2d at 98, that:

²This contention finds no support in the language of Section 5, which makes it “unlawful for *any person*, directly or indirectly * * * to sell unregistered securities (emphasis added).

³We are not aware of any case holding that an injunction may not be predicated on a person’s aiding or abetting a securities violation. *Timetrust v. Securities and Exchange Commission*, 142 F. 2d 744, 746 (C.A. 9), upon which petitioner relies (Pet. 11), reversed a district court’s injunction against certain aiders or abettors because there was “no evidence that they participated in any way in the selling campaign.” None of these defendants was an attorney who gave an opinion as to the validity of the securities sales involved. See *Timetrust v. Securities and Exchange Commission*, 130 F. 2d 214, 215 (C.A. 9).

[T]raditionally in equity, where there is a right to issue a general injunction in a situation, the court has the power inherently to impose upon any persons, who have contributively played a part in the doing or committing of the enjoined action involved (where they are made party to the suit), such reasonable and relevant individual restraint as may be necessary to enable the decree to accomplish its preventive purpose. * * *

Thus, as the court of appeals noted in the instant case (Pet. App. 6a):

In order to accomplish the broad remedial purposes of the Securities Acts, *Affiliated Ute Citizens of Utah v. United States*, 406 U.S. 128, 151 (1971), there are compelling reasons to impose secondary liability in Section 5 actions. By its terms, Section 5 makes it unlawful, “directly or indirectly”, to sell unregistered stock. The heart of this prohibition would be cut away if the only person covered by its provisions was the individual who actually consummated the sale.

Petitioner relies (Pet. 9) upon a footnote in *Ernst & Ernst v. Hochfelder*, 425 U.S. 185, 191-192 n. 7, in which this Court stated:

In view of our holding that an intent to deceive, manipulate, or defraud is required for civil liability under §10(b) and Rule 10b-5, we need not consider whether civil liability for aiding and abetting is appropriate under the section and the Rule, nor the elements necessary to establish such a cause of action. * * *

The *scienter* requirement which the Court in *Ernst & Ernst* held to be applicable to actions brought pursuant to Section 10(b) and Rule 10b-5, which deal with deception, manipulation, and fraud, is inapplicable in an action

under Section 5. As the court of appeals correctly observed (Pet. App. 6a), *Ernst & Ernst* does not suggest "that those who play an indispensable role in the sale [of securities without registration], as [petitioner] did here, should not be subject to SEC initiated, injunctive restraint." "No intent is required to violate Section 5 as an aider and abettor * * *." *Securities and Exchange Commission v. National Bankers Life Insurance Company*, 324 F. Supp. 189, 194 (N.D. Tex.), affirmed 448 F.2d 652 (C.A. 5); see also *Securities and Exchange Commission v. International Chemical Development Corp.*, 469 F.2d 20, 33-34 (C.A. 10); *Nees v. Securities and Exchange Commission*, 414 F.2d 211, 220 (C.A. 9).

Moreover, even if the *scienter* requirement of *Ernst & Ernst* were to apply to an injunctive action under Section 5, petitioner's conduct demonstrated *scienter*. As the court of appeals observed (Pet. App. 7a), its "decision need not rest on [its] rejection of [petitioner's] negligence-scienter argument, because the District Court found that [petitioner] in some circumstances knew and in other circumstances had reason to know that his client was engaging in illegal transactions with the aid of [petitioner's] letters and that [his] acts were performed with knowledge or reckless disregard of the truth."

2. Petitioner also contends (Pet. 14-18) that an injunction was not warranted because the Commission did not demonstrate a reasonable likelihood that petitioner's violations would be repeated. Both courts below found to the contrary, however⁴ (Pet. App. 9a, 49b-50b).

⁴Contrary to the undocumented statements in the petition, the Commission has not "conceded that there was absolutely no likelihood of any future securities laws violation by this defendant" (Pet. 8), or "no reasonable likelihood of future securities law violations by the defendant" (Pet. 14).

CONCLUSION

For the foregoing reasons the petition for a writ of certiorari should be denied.

Respectfully submitted.

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